

**AGREEMENT RELATING TO
WATER DELIVERY TO
MOUNTAINSTAR RESORT
between the
CITY OF CLE ELUM,
TRENDWEST RESORTS, INC.,
TRENDWEST INVESTMENTS, INC.,
and
MOUNTAINSTAR RESORT RESOURCES, INC.**

THIS AGREEMENT is entered into this 19th day of JUNE, 2001, between the City of Cle Elum, a second-class municipal corporation organized under the laws of the State of Washington (hereafter "City"), Trendwest Resorts, Inc., an Oregon Corporation, Trendwest Investments, Inc., a Washington corporation, and MountainStar Resort Resources, Inc. ("MRR"), a Washington Corporation (hereafter collectively "Trendwest").

RECITALS:

1. The City is a second-class city organized under the laws of the State of Washington, located in Kittitas County, Washington, and is authorized by RCW 36.70A.360(2) and City Resolution No. 3/14/00-1, through its Mayor with the approval of its City Council, to enter into agreements associated with the diversion, treatment and delivery of water to Trendwest property outside the City.
2. The City, in cooperation with the Town of South Cle Elum and with the guidance and encouragement of the Washington State Department of Ecology and the Washington State Department of Health, is in the process of developing a new regional public water supply system (hereafter "WSS") that is designed to provide water to users within the City and the Town as well as other users on lands located nearby.
3. Trendwest conducts residential, commercial, and recreational development activities upon real property, and is authorized, through its officers, to execute this agreement.
4. Trendwest is the owner of approximately 6,200 acres, known as the MountainStar property, located near the City of Cle Elum, Kittitas County. Trendwest is proposing a Master Planned Resort (hereafter "MPR") consisting of, among other elements, hotel, commercial, residential, golf course, and equestrian facilities, and open space. Exhibit A attached hereto sets forth on a map the MPR.
5. Trendwest needs water to serve the MPR and in 1997 approached the City with a request that the City deliver water (to be derived from the exercise of water rights or supplies owned by Trendwest as described in Section 7 or otherwise authorized for

Trendwest's use) through the City's WSS to pipelines and related facilities of Trendwest which would be connected to the City's WSS.

6. In response to the water delivery request of Trendwest, the City conducted a series of public meetings (before both a Committee of the City Council and the City Council) during 1998, 1999, and 2000 related to the establishment of a City policy pertaining to water use within the MPR. On March 14, 2000, the City adopted Resolution No. 3/14/00-1. The foundation City policy set forth in the Resolution states that "no existing water rights or supplies presently owned by the City shall provide the base for supplying water to the MPR." The Resolution further provides, among its elements, that the City will not deliver water to the MPR until a water supply agreement consistent with the policy and requirements of the Resolution is executed by the City and Trendwest.

7. Trendwest now owns significant water rights related to the Yakima River system (and may acquire additional water rights or water supplies in the future). As to a portion of these water rights, Trendwest has requested, pursuant to RCW 90.03.380, that its rights be changed (1) as to point of diversion to a water diversion (intake) facility of the City of Cle Elum, (2) as to place of use to the MPR, and (3) as to purpose of use to domestic and irrigation uses.

8. Trendwest has formed and owns a utility company, MountainStar Resort Resources, Inc. ("MRR"), which will set water rates and provide water service within the MPR, subject to regulation by the Washington Utilities and Transportation Commission.

9. Trendwest's desire is for the City to divert, treat, and convey through the WSS all or a portion of the water derived from the exercise of the rights and supplies owned by Trendwest (as described in Section 7 or otherwise authorized for Trendwest's use) to Trendwest for service within the MPR. Trendwest proposes to pay the City for reasonable and necessary costs associated with the diversion, treatment, and delivery of water through the City's WSS.

10. The City is willing to deliver water, as described in Section 7, to the MPR consistent with Resolution No. 3/14/00-1 on a long term stable supply basis through the City's WSS. In relation thereto, the City has entered into a Cost Allocation Agreement on _____ with Trendwest relating to financing of construction of the City's WSS.

11. It is the purpose of this Agreement to satisfy the requirement of Section 3 of the aforementioned City's water right/supply policy, Resolution No. 3/14/00-1, that a water agreement be executed between the parties before any water is delivered to the MPR by the City.

AGREEMENTS:

On the basis of Recitals 1 through 11, the City and Trendwest agree as follows:

12. **Delivery of Trendwest Water.** The City agrees to deliver water to one or more of the MPR water supply connection facilities, when requested by Trendwest.

A. Water delivered to the MPR shall:

1. Be based solely on water rights or other water supplies owned or authorized for use by Trendwest, and any exercise of said rights or supplies of Trendwest shall:
 - (a) be undertaken only after compliance with applicable state and federal laws, including any approval of required changes pursuant to RCW 90.03.380 or RCW 90.44.100 or Chapter 90.80 RCW, and any other government agency or court approval required prior to the exercise of the changed right;
 - (b) not, after being approved for change of rights or supplies, be exercised in a manner in which the change of use will impair the ability to exercise to their fullest extent the existing water rights or supplies of the City and the Town of South Cle Elum, whether they be based on rights that are junior or senior in priority; and
 - (c) not change the priorities of existing rights to divert water from the Yakima River or its tributaries.
2. Not exceed in total the amounts, both in acre-feet yearly (afy) and instantaneous (cfs), approved as provided in Section 12 (A)(1)(a), above, less conveyance and treatment losses associated with operation of the City facilities in delivering water to the MPR.

B. Except as provided in Subsection (3), below, or as provided in Section 16, no water shall be delivered to the MPR:

1. Prior to necessary approvals as provided in Section 12 (A)(1)(a), above;
2. Prior to the approval by the Washington State Department of Health of the water supply system for the MPR;

3. Prior to completion of the City's new regional WSS, including water diversion, treatment, and conveyance facilities, in an approved operating condition to the extent required to supply water to the various elements of the MPR; provided that nonpotable water may be delivered before treatment facilities are completed.
- C. Nothing in this Agreement shall preclude Trendwest from providing water to serve the MPR by (1) obtaining additional water supplies or (2) delivering water from diversion and delivery facilities other than the City's WSS, provided that Trendwest shall be responsible to pay for any WSS operation and maintenance costs which exceed the operation and maintenance costs that would have been incurred by the City if the City had constructed only the water supply system described in the Cle Elum- South Cle Elum Comprehensive Water Plan, dated October 1997, unless and to the extent such costs are later assumed by other future users.

13. **Delivery Charges.** Trendwest agrees to pay the City for reasonable and necessary costs associated with delivery of water, on a monthly basis and in accordance with charges adopted by the City specifically for the delivery of water, both potable (treated) and non-potable (untreated), from the City WSS to any water conveyance facilities owned by Trendwest connected to the WSS for conveyance by Trendwest of water to and within the MPR. Charges shall be specifically established by the City for (1) potable (treated) and (2) non-potable (untreated) water delivered to the Trendwest water supply system connection facilities in accordance with the following:

- A. The charges shall be based on the following criteria:
 1. Operation and maintenance costs related to the delivery of water to Trendwest's water supply connection facilities, including but not limited to operation, maintenance, energy, and chemical costs.
 2. Eventual replacement of a proportionate share of the WSS facilities and equipment used to divert, treat and deliver water to the MPR. Therefore, the charges shall provide for recovery of a proportionate share of costs to (a) fund a capital reserve account and/or (b) provide debt service and debt service coverage if required, which may be incurred by the City to borrow money to replace such facilities and equipment in the future. The balance between funding capital replacement from cash in a capital reserve account or from using debt shall be determined in the study described in Subsection 13 (D), below.

3. Reasonable administrative costs of the City associated with providing water diversion, treatment (when required), and delivery to the MPR.
 4. Separate charges shall be calculated for both treated and non-treated water to be supplied under the terms of this agreement.
 5. The charges shall:
 - (a) be based on actual metered flows delivered by the City WSS to the MPR, measured at Trendwest's water system points of connection with the WSS, and shall be designed to achieve proportionate sharing of the costs of water diversion, treatment (when required), and delivery; and
 - (b) reflect, to the extent not covered in Section 13(A)(5)(a) and Section 22, a minimum monthly base charge regardless of actual flows delivered, including months where none is delivered, to pay for any incremental operation and maintenance costs resulting from increased sizing of the City's water facilities to serve the MPR, as described in Section 12(C).
- B. The obligation of Trendwest to pay the City for delivery of non-potable and potable water shall commence on the date the City certifies in writing to Trendwest that the City is able to deliver such water.
- C. The City shall use the following procedure for the establishment of charges as provided in the first paragraph of this section. Prior to the adoption of such charges, the Mayor, with the approval of the City Council, shall engage the services of a consultant, with appropriate experience and credentials in recommending water utility rates, for the purposes of (1) the development of proposed charges based on the criteria set forth in Subsection A of this section, (2) the submission of a written report to the Council setting forth recommended charges and the analysis supporting the same, and (3) a presentation to the Council on said written report. The consultant shall be selected by the Council after consultation with Trendwest. Trendwest agrees that it will reimburse the City for all costs incurred by the City including obtaining the aforescribed services as well as any additional costs incurred by the City which would not have been incurred except for the need to adopt charges as provided by this section.

- D. The initial charges adopted by the City based on the report of the consultant shall be subject to review by the City following the water system startup period, and the initial charges shall be adjusted, if necessary, based on actual operating experience.
- E. The City may periodically increase charges. Increases shall be reasonably related to increased costs incurred by the City to deliver water as provided in this Agreement. The City shall consult in advance with Trendwest regarding any water charge increases proposed in the future. If Trendwest disagrees with the terms or provisions of proposed water charge increases, Trendwest may request a full study, at its expense, to assess the reasonableness and necessity of proposed charge increases. The City shall consider the results of such a study before enacting any charge increases, provided, however, that Trendwest shall have no veto authority over increases established by the City. In the event that this charge increase process results in continued disagreement between the City and Trendwest after the City enacts an increase, the provisions of the Mediation and Arbitration Agreement, dated December 7, 1999 shall be used to resolve the disagreement.
- F. No connection fees or charges shall be assessed by the City for the delivery of water to the MPR.

14. **City Representations and Warranties.** The City makes the following representations and warranties to Trendwest:

- A. It is vested with the power and authority and has taken all implementing actions necessary to enter into this Agreement.
- B. It shall design, construct, operate, and maintain points of diversion (water intake facilities) from the Yakima and Cle Elum Rivers and a water treatment and delivery system (together, the WSS as defined in Section 2, above) (1) in compliance with all applicable laws and regulations as they pertain to public water supply systems, (2) adequate for the diversion, treatment and delivery of water for any of the MPR water uses contemplated by this Agreement, not to exceed the amounts described in Section 12(A)(2) and consistent with the phasing provisions of the Cost Allocation Agreement referred to in Section 24(A), and (3) consistent with all reasonably necessary and appropriate controls and safety measures to ensure that such connection(s) do not damage or contaminate the MPR water system or the MPR water supplies or sources.

- C. It shall not grant, now or in the future, to any other comparable class of wholesale water user, any rights, charges, or rate schedules more favorable than those provided for in this Agreement without also making the same available to Trendwest.
- D. It shall not enter any agreement with any third party that detrimentally affects Trendwest's water rights or other water supplies or Trendwest's rights relied upon for delivery of water under this Agreement without Trendwest's express written consent, which consent may be withheld in Trendwest's sole discretion.
- E. It shall not impose any conditions, restrictions or limitations, except as required by State or Federal law or as provided in Section 12(A)(1)(b), that affects Trendwest's water rights or other water supplies or Trendwest's rights under this Agreement without Trendwest's express written consent, which consent may be withheld in Trendwest's sole discretion.
- F. It shall notify MRR and appropriate Trendwest MPR operations personnel in advance, when so known, or as soon as reasonably practical after learning of the same, as to any event that may result in a reduction, interruption or delay in the City's ability to fully perform under this Agreement, and, in the event a matter of public health or safety is involved, such notice shall be immediate.
- G. It shall not knowingly take any actions harmful to any of Trendwest's efforts to obtain water for use within the MPR, unless such efforts by Trendwest would otherwise be determined by the City Council to be detrimental to the public health, safety and welfare of the City, including its water rights and other water supply sources.

15. **Trendwest Representations and Warranties.** Trendwest makes the following representations and warranties to the City:

- A. It is vested with the power and authority and has taken all actions necessary to enter into this Agreement.
- B. It shall take all reasonable and appropriate steps when requested by the City to make available to the City water derived from Trendwest-owned water rights or any other water supplies of Trendwest which are authorized for diversion at a City WSS intake facility, for use within the City service area when needed to respond to an emergency affecting public health or safety not covered by the provisions of Section 17 and 18(b).

- C. It shall design, construct, operate and maintain those parts of its water system that are connected to any portion of the City WSS in compliance with all applicable laws and regulations and consistent with all reasonably necessary and appropriate controls and safety measures to ensure that such connection(s) do not damage or contaminate the City WSS or its water supplies or sources.
- D. It shall notify the City in advance, when so known, or as soon as reasonably practical after learning of the same, as to any event that may adversely impact the City WSS or Trendwest's ability to fully perform under this Agreement, and, in the event a matter of public health or safety is involved, such notice shall be immediate.

16. **Interim Water Delivery.** Notwithstanding any provision of this Agreement, water may be delivered by the City to the MPR from the existing City system, to the extent and in an amount as determined by the Council of the City in its sole discretion if:

- A. Existing City facilities are physically capable of diverting, treating and/or delivering water to the MPR; and
- B. Water rights have been approved as provided in Section 12 (A)(1)(a) of this Agreement, or otherwise made available by Trendwest for diversion at an existing river diversion facility; and
- C. A written agreement between the City and Trendwest, including interim charges, is executed prior to any delivery.
- D. As to water supplied to the MPR for domestic use, in addition to the restrictions of 16.A-C, above, none shall be supplied until:
 - 1. A comprehensive water system plan relating to the public water supply system for the MPR has been approved by the Washington State Department of Health; and
 - 2. All other governmental permits and other approvals, required before said MPR system may deliver water for such use, are obtained.
- E. As to interim water delivered to the MPR for golf course uses, Trendwest agrees to use all reasonably available water saving equipment and facilities as well as methods of operation, in order to achieve the most efficient use of water thereon.

17. **Reduction in WSS Functional Capacity.** In the event City WSS capacity as it pertains directly to the City's ability to meet its obligations to deliver water under this

Agreement is significantly and adversely reduced as a result of a change in operating condition, Trendwest and the City agree to cooperate and coordinate to reduce the water use of each consistent with the estimated term of reduced WSS capacity, available storage capacities, and fire flow requirements. The parties shall proportionately share the capacity reduction based upon their then-current demand for treated and untreated water (giving due regard to whether the operating condition relates to either or both); provided that the highest priority, in rank of priority of use, shall be the parties' respective uses for (1) emergencies associated with the protection of public health and safety, essential services, e.g., hospital and fire, and in-home domestic use, and (2) maintenance of essential economic activities, including commercial uses and irrigation of golf course tees and greens.

18. **Water Shortages.** In the event of a water shortage, the parties agree, taking into account the current needs for water of each, to reduce the use of water during the term of the water shortage in the following manner. If a water shortage is determined to exist, the City and Trendwest shall implement water use reduction measures applicable to uses of water within their service areas with the highest priority of water in rank of priority of use, supplied for (1) emergencies associated with the protection of public health and safety, essential services such as hospital and fire, and in-home domestic use, and (2) maintenance of essential economic activities, including commercial uses and irrigation of golf course tees and greens.

- A. For purposes of this Section 18, a "water shortage" is defined as a condition wherein water is not available to the City for diversion through its facilities (1) due to the insufficiency of public waters available for diversion or (2) because of a forecast of such insufficiency in the near future based on basin-wide water availability forecasts; said "water shortage" to be determined by either:
 - 1. The Washington State Department of Ecology (or other governmental entity with authority if any there may be) issuing a directive restricting the amount of water diverted by the City; or
 - 2. The City, after consultation with the United States Bureau of Reclamation, concluding that there is an insufficiency of water available for diversion by the City as hereinbefore described.
- B. If during the course of a water shortage (1) water rights or other supplies of the City are not sufficiently exercisable to satisfy the aforescribed highest priority uses within the City and (2) any water rights or supplies owned by Trendwest and delivered through a City diversion works are exercisable, these rights of Trendwest shall, to the extent authorized by law, be exercised so as to meet the high priority uses, based on the then existing needs of the City's service area and the

MPR, so as to satisfy such uses on a proportional basis within both the MPR and the City's service area.

19. **Trendwest Indemnity.** Trendwest shall indemnify and hold harmless the City, its elected and appointed officials, employees, and agents, and their successors and assigns, from any and all claims arising under or related to the representations and warranties given by and the undertakings of Trendwest to the City in this Agreement, including, but not limited to, claims pertaining to the exercise of Trendwest water rights or water supplies and supporting the delivery of water to the MPR, except to the extent the claims are based exclusively on the negligence of the City and the defense of sovereign immunity does not apply. This indemnity shall survive cancellation of the agreement.

20. **City Indemnity.** The City shall indemnify and hold harmless Trendwest, its officers, directors, employees, and agents, and their successors and assigns, to the extent authorized by law, from any and all claims arising under or related to the representations and warranties given by and the undertakings of the City to Trendwest in this Agreement, except to the extent the claims are based exclusively on the negligence of Trendwest.

21. **Trendwest Reimbursement of Other City Costs.** Trendwest shall reimburse the City for all costs reasonably incurred by the City (a) in defending the validity or exercisability of all water rights changed to the City's diversion works involved in the Acquavella general adjudication or in any "non-general adjudication" of water rights litigation or in any other governmental action or process which may affect the legal status and/or the ability to exercise Trendwest water rights or water supplies, including putting water to a beneficial use; (b) while participating in any federal, state, or local water planning process, including among others, habitat conservation planning relating to federal Endangered Species Act listings, which may affect the legal status and/or the ability to make beneficial use of Trendwest's water rights or water supplies, or participation therein is the direct result of the City's obligations under this Agreement; or (c) in defending the validity of this Agreement, other than for procedural errors by the City made during the course of the approval by the City of this Agreement.

22. **Termination.** As the supply of water to Trendwest and the MPR is indispensable, the City cannot terminate this Agreement except upon the agreement of Trendwest. Trendwest may terminate this Agreement upon 60 days written notice to the City, provided that Trendwest or its successors, if any, shall remain responsible to pay the City for any water system operation and maintenance costs following such termination resulting from increased sizing of the WSS to deliver water to the MPR, as described in Section 12(C).

23. **Binding Effect.** This agreement is binding upon and inures to the benefit of the parties to this Agreement as well as upon and to the benefit of their respective heirs, personal representatives, assigns, and other successors in interest. It is specifically contemplated that Trendwest may transfer ownership of portions or all of its MPR properties

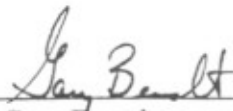
in Kittitas County to other entities and individuals that will also expect and require a reliable water supply.

24. **Entire Agreement; Relationship to Other Agreements.** There are no agreements, promises, assurances, representations, warranties, undertakings, or understandings, either written or oral, between Trendwest and the City concerning the subject matter of this Agreement other than those expressly set forth in this document. Any amendment of this Agreement must be in writing and signed by both the City and by Trendwest.


- A. The parties have previously executed other agreements concerning Trendwest's anticipated projects, some of which deal with the subject of water and including, but not limited to, the Agreement for Payment of Professional/Staff/Consultant Services, the Pre-Annexation Agreement, and the Cost Allocation Agreement. This Agreement does not amend or supersede any other agreement between the parties. This Agreement is intended to be consistent with the terms of such other agreements, but to the extent of any conflict with those other agreements, the terms of this Agreement shall control as to issues relating to the delivery of water to Trendwest for the MPR under this Agreement.
- B. The parties expressly agree that this Agreement incorporates by this reference the Mediation and Arbitration Agreement dated and executed by the parties on December 7, 1999; provided, however, that the provisions of the Mediation and Arbitration Agreement to the contrary notwithstanding, in the event of a dispute involving water supply or water delivery which, in the reasonable opinion of either party, requires an interim or permanent resolution in a more expeditious timeframe, either or both parties may apply to the Superior Court of Kittitas County for specific performance or injunctive or other relief; and provided, further, however, that any relief requested by a party from the court shall include a request that the Court order be fashioned to the extent reasonably possible to allow the matter to be concluded under the terms of the Mediation and Arbitration Agreement.

Dated as of the day and year first above written.

City of Cle Elum

By 
Gary Berndt
Mayor


Trendwest Resorts, Inc.

By 
President

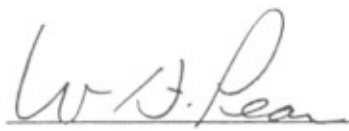
Approved as to form:


Erin Anderson
City Attorney

Trendwest Investments, Inc.

By 
President

MountainStar Resort Resources, Inc.

By 
President